**Office of Chief Counsel**
**Internal Revenue Service**

# memorandum

CC:LM:HMT:CLE:POSTF-113441-02
RSBloom

date: May 28, 2002

to: LMSB:NR: [redacted]
Attn: [redacted]

from: Associate Area Counsel, LM:HMT:CLE

subject: [redacted]
**Audit/TEFRA Concerns**
**Years [redacted] - [redacted]**

This memorandum responds to your various requests for advice made during March and April, 2002, regarding issues being encountered in the closure of the [redacted] through [redacted] examination years of the above-referenced partnership. This memorandum should not be cited as precedent. The advice contained in this memorandum is subject to 10-day post review by our National Office and, therefore, is subject to modification.

**ISSUES**

1) If some or all the partners sign a Form 870-P for all partnership items, can the partnership or a partner in either its partner or corporate entity status file a protective claim pending a change in the [redacted] opinion.

2) What are the ramifications to the partners and the Service if the Service solicits and obtains partial agreement Forms 870-P from only a portion of the partners.

3) Are there any consequences if the Service enters into closing agreements, wherein it is agreed that there are no deficiencies or overpayments for the years [redacted] through [redacted], with the 3 partners with the smallest partnership interests.

4) With respect to the years [redacted] and [redacted], are the statutes of limitations open for purposes of assessing partnership item adjustments and/or filing AAR suits.

5) If no action is taken for certain partners with respect to their partnership interests for the years [redacted] to [redacted], would there be any consequences to Exam with respect to the non-[redacted] claim issues for the years [redacted] to [redacted].

## CONCLUSIONS

1) If all the partners sign a Form 870-P for all partnership items, neither the partnership nor any partner retains any interest in the partnership matters for the agreement years. There is no protective claim that can be filed to await the appeal of [redacted], and the partners cannot benefit from any future change in the [redacted] opinion.

If some, but not all, partners sign a Form 870-P for all partnership items, the partners that do not sign a Form 870-P covering the [redacted] ([redacted]) issue can possibly benefit from a change in the [redacted] opinion. Although a protective claim cannot be filed by these partners, the issue nevertheless will remain alive for awhile due to the extension of the statute of limitations on assessment and/or the filing by the tax matters partner of Forms 8082.

2) If the Service solicits and obtains partial agreement Forms 870-P from only a portion of the partners, the remaining partners have the right, for a period of time, to request consistent settlement terms. The Service will have to decide whether to issue an FPAA for the years [redacted] through [redacted]. If an FPAA is not issued, the tax matters partner will have to decide whether to petition with respect to the AARs filed for the years [redacted] through [redacted]. Whether or not an FPAA is issued, the tax matters partner will also have to decide whether to petition with respect to the AARs filed for the years [redacted] and [redacted].

3) If the Service enters into closing agreements with the 3 partners with the smallest partnership interests, the remaining partners can request settlement on consistent terms.

4) The statute of limitations for assessing partnership item adjustments for the years [redacted] and [redacted] has expired. However, the statute of limitations for petitioning from the AARs filed for the years [redacted] and [redacted] has been extended by agreement to [redacted].

5) If no action is taken for certain partners with respect to their partnership interests for the years [redacted] through [redacted], the Service can still audit all partnership items for the years [redacted] to [redacted]. The partnership audit is a separate and distinct audit from that of the partners.

**FACTS**

[redacted]

Notices of beginning of an administrative proceeding at the partnership level ("NBAP") with respect to partnership items of the above-named partnership were mailed as follows:

| YEAR | DATE MAILED |
|---|---|
| [redacted] | [redacted] |

On [redacted], during the course of the [redacted] through [redacted] examinations of [redacted], Forms 8082, Amended Return (Administrative Adjustment Request (AAR)), were filed by the tax matters partner for the partnership. The forms requested additional deductions for [redacted] in the amounts of $[redacted] in [redacted] and $[redacted] @ year in [redacted] through [redacted]. Forms 872-P, "Consents to Extend the Time to Assess Tax Attributable to Items of a Partnership," have been timely executed, extending the time in which to assess partnership items for the partnership years [redacted] through [redacted] to [redacted].

Forms 8082 were filed by the partnership for the years [redacted] and [redacted] before any examination proceeding for such years had commenced. The [redacted] partnership return was filed [redacted]. For [redacted], the Form 8082 was filed [redacted]; it claimed additional [redacted] deductions in the amount of $[redacted] (accruing a deduction for future estimated [redacted] costs) and a reduction of depreciation expense in the amount of $[redacted] (carrying-over prior year adjustments to the useful lives of

depreciable assets). For [redacted], the partnership return was filed [redacted]. The Form 8082 for such year was filed [redacted]; it claimed additional [redacted] deductions in the amount of $[redacted] (accruing a deduction for future estimated [redacted] costs) and a reduction of depreciation expense in the amount of $[redacted] (carrying-over prior year adjustments to the useful lives of depreciable assets). Forms 9248, "Agreements to Extend the Time to File a Petition for Adjustment by the Tax Matters Partner (Person) With Respect to Partnership or Subchapter S Items," have been timely executed, extending the time in which the partnership may bring suit with respect to the filed AARs for the years [redacted] and [redacted] to [redacted]. No Forms 872-P have been executed with respect to the partnership for the years [redacted] and [redacted]. Forms 872, "Consents to Extend the Time to Assess Tax," extending the period in which to assess the income tax of [redacted], the common parent of two of the principal partners [redacted], and [redacted] for the years [redacted] and [redacted] were executed; however, these consents did not expressly cover partnerships and, in any event, only extended the statutory period for assessment to [redacted].

During the course of the [redacted] through [redacted] examinations, Forms 8082, requesting additional deductions for [redacted] in the amount of $[redacted] for each year, were filed by the partnership. The Forms 8082 for the years [redacted], [redacted] and [redacted] were filed on [redacted], [redacted], and [redacted], respectively. Forms 872-P were timely filed, extending the time in which to assess partnership items for the years [redacted] through [redacted] to [redacted].

Examination took no action on the [redacted] claims contained in the Forms 8082 because [redacted]. On [redacted], the Tax Court issued an opinion favorable to the Service on the [redacted] issue for pre-TEFRA years in [redacted]. Since other issues in the [redacted] case are still pending before the Tax Court, no decision has been filed in the Tax Court case from which an appeal can be filed. The [redacted] claims range, in total over the years [redacted] through [redacted], per partner from a high of $[redacted] to a low of $[redacted].

Representatives of [redacted]'s tax matters partner have indicated that they have been in contact with the [redacted] partners, other than the [redacted] partners (who allegedly cannot be located), and, with respect to the years [redacted] through [redacted], the partners are in agreement with all examination issues except the disallowance of

the additional [redacted] claimed on the Forms 8082. The examination issues (excluding disallowed [redacted] claims) range, in total over the years [redacted] through [redacted], per partner from a high of $[redacted] to a low of $[redacted]. For the 3 partners (other than the [redacted] partnerships) with the smallest partnership interests [[redacted], [redacted], and [redacted]], the examination issues (excluding disallowed [redacted] claims) range, in total over the years [redacted] through [redacted], from $[redacted] to $[redacted].

The [redacted] partners were partners in [redacted] for only [redacted] of the years in issue, [redacted] and [redacted]. Since the number of 2nd tier partners through the [redacted] partnerships were so numerous and the proposed adjustments were individually de minimus, no action was taken to link the 2nd tier partners. The total of the unagreed [redacted] claim adjustments for the [redacted] years [redacted] and [redacted] relating to the [redacted] partnerships range from $[redacted] to $[redacted]. The total for the [redacted] years of the other examination adjustments range from $[redacted] to $[redacted]. For the partner with highest adjustment, the $[redacted] adjustment is broken down as follows: $[redacted] for [redacted] and $[redacted] for [redacted].

With respect to the [redacted] through [redacted] years, there are some unresolved issues in addition to the [redacted] issue; therefore, the parties wish to proceed at this time with the resolution of only the years [redacted] through [redacted].

**LAW and ANALYSIS**

The tax treatment of any partnership item shall be determined at the partnership level. I.R.C. § 6221. Partnership items are those items required to be taken into account for the partnership's taxable year which are more appropriately determined at the partnership level. I.R.C. § 6231(a)(3). The [redacted] costs as well as the depreciation deductions in issue clearly constitute partnership items. Treas. Reg. § 301.6231(a)(3)-1(a)(1)(i). The term partnership means any partnership required to file a return under section 6031(a), which is not a small partnership. I.R.C. § 6231(a)(1)(A)&(B). For the years in issue, a small partnership was a partnership having 10 or fewer partners each of whom was a natural person (other than a nonresident alien) or an estate. I.R.C. § 6231(a)(1)(B)(i). Since the partnership in question did not qualify as a small partnership (more than 10 partners, all of whom were corporations or partnerships), the TEFRA partnership rules apply.

A settlement between the Service and 1 or more partners in a

partnership with respect to the determination of partnership items for any partnership taxable year shall (except as otherwise provided in such agreement) be binding on all parties to such agreement with respect to the determination of partnership items for such partnership taxable year. I.R.C. § 6224(c)(1). Form 870-P, Agreement to Assessment and Collection of Deficiency in Tax for Partnership Adjustments, is the form used to reflect such a settlement. As indicated in the above parenthetical, a settlement is binding with respect to the determination of partnership items for the partnership taxable year **except as otherwise provided in such agreement**. In other words, a settlement does not have to settle all partnership items of a partnership for the taxable year; the parties can enter into a partial settlement. See Treas. Reg. § 301.6224(c)-3(a).

If the Service enters into a settlement agreement with any partner with respect to partnership items for any partnership taxable year, the Service shall offer to any other partner who so requests[1] settlement terms for the partnership taxable year which are consistent with those contained in such settlement agreement. I.R.C. § 6224(c)(2). This provision applies whether the settlement is comprehensive or partial. Treas. Reg. § 301.6224(c)-3(a). Therefore, if the Service solicits and obtains partial agreement Forms 870-P from only a portion of the partners, the remaining partners have the right to request consistent settlement terms. Likewise, if the Service resolves the partnership items in their entirety with the 3 partners with the smallest partnership interests by entering into a closing agreement (reflecting no deficiencies or overpayments), the remaining partners have the right to a consistent settlement. In either case, the other partners must make their request[2] no later than the later of (i) the 150th day after the day on which the notice of final partnership administrative adjustment is mailed to the tax matters partner; or (ii) the 60th day after the day on which the settlement agreement was entered into. Treas. Reg. § 301.6224(c)-3(c)(3).

The partnership items of a partner for a partnership taxable

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[1]It is the tax matters partner's responsibility to furnish the partners with information regarding the Service's acceptance of any offer. I.R.C. § 6223(g); Treas. Reg. § 301.6223(g)-1(b)(1)(iv).

[2]The request must be in the form of a written statement to the IRS office that entered into the settlement. The required content of the statement is set forth in Treas. Reg. § 301.6224(c)-3(c)(2).

year become nonpartnership items as of the date the Service enters into a settlement agreement with the partner with respect to such items. I.R.C. § 6231(b)(1)(C).[3] Therefore, once a partner settles all partnership items for a partnership taxable year, he no longer has an interest in any partnership matter relating to partnership items for that partnership taxable year. Under section 6226(d)(1), a partner that settles partnership items with respect to a partnership taxable year cannot be a party to any judicial review of a notice of final partnership administrative adjustment ("FPAA") relating to the settled partnership items. He also cannot file a readjustment petition with respect to such a notice regarding settled partnership items. I.R.C. § 6226(d)(2). Likewise, he cannot be a party to any judicial review of the disallowance in whole or in part of an administrative adjustment request relating to settled partnership items. I.R.C. § 6228(a)(4)(B). Thus, if a partner settles all partnership items for a partnership year, he cannot participate in any judicial review of any partnership matter relating to that year. Consequently, if all partners sign a Form 870-P for all partnership items, neither the partnership nor any partner may take any action with respect to the [redacted] partnership issue in the event there is ultimately a change in the [redacted] opinion. However, if only some of the partners sign a Form 870-P for all issues, the partnership through the tax matters partner and possibly the other partners, depending upon the Service's actions,[4] may take action with respect to the [redacted] partnership issue.

If all the partners do not sign a Form 870-P for all partnership items[5], the Service ultimately has two choices. It can either issue to the tax matters partner an FPAA or do nothing and permit the statute of limitations on assessment to expire.[6]

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[3]Once the items become nonpartnership items due to a comprehensive settlement, a 1-year statute of limitations for assessment with respect to the settling partner is triggered. I.R.C. § 6229(f)(1). However, this 1-year statute of limitations is not triggered when there has only been a partial settlement of partnership items. I.R.C. § 6229(f)(2).

[4]As discussed below, the Service has a choice from 2 courses of action.

[5]If all partners sign a Form 870-P for all partnership items, the partnership matter is resolved.

[6]The Service is not required to issue an FPAA for unagreed partnership item adjustments. Atlantic Richfield Co. v. United

If the FPAA is issued, the tax matters partner has 90 days in which to petition for a readjustment. I.R.C. § 6226(a). If the tax matters partner does not file a petition, any notice partner[7] may, within 60 days after the close of the 90-day period for the tax matters partner to petition, file a petition for a readjustment. Thus, if the Service chooses to issue an FPAA, the tax matters partner can file a petition on behalf of the partnership. If the tax matters partner does not file a petition, a partner that has not settled all partnership items can petition. A court with which a petition from an FPAA is filed has jurisdiction to determine **all partnership items of the partnership for the partnership taxable year to which the FPAA relates**. I.R.C. § 6226(f).

The general statute of limitations for assessing any tax with respect to any person which is attributable to any partnership item is 3 years from the later of the date on which the partnership return was filed or the last day for filing such return (without regard to extensions). I.R.C. § 6229(a). This 3-year period can be extended by agreement. I.R.C. § 6229(b).[8] Under the present facts, Forms 872-P have been timely executed by the tax matters partner, extending the statutory period for the years [redacted] through [redacted] to [redacted]. These Forms 872-P extend the period for all partners. However, no Form 872-P was executed by the tax matters partner for the years [redacted] and [redacted]. Also, the partners did not individually enter into agreements to extend the statutory period for the years [redacted] and [redacted]. Thus, the assessment period for the [redacted] through [redacted] tax years presently expires [redacted]. However, for the years [redacted] and [redacted], the period has expired.

Although the Forms 9248, which were executed with respect to the years [redacted] and [redacted], mention the depreciation adjustments, they do not extend the statutory period for assessment purposes. However, to the extent the partnership brings an action in court for a judicial review of the disallowance of, or non-action with regard to, the administrative adjustment requests, the Service

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States, 97-1 U.S.T.C. ¶ 50,170 (D NH 1996); Treas Reg. § 301.6223(a)-2(a).

[7]A notice partner is defined in section 6231(a)(8). Notice partners receive copies of the FPAA. I.R.C. §§ 6223(a)(2) and (d)(2).

[8]It can be extended for all partners by the tax matters partner or with respect to any partner by agreement with such partner. I.R.C. § 6229(b)(1)(A)&(B).

can assert as offsets in the proceeding the depreciation adjustments for which assessment is barred. I.R.C. § 6228(a)(5). The offset is merely available to reduce or eliminate the adjustment claimed by the partnership; it may never give rise to a judgment in favor of the Government. See Patterson v. Belcher, 302 F.2d 289 (5th Cir. 1962), which was a case involving a claim for refund of income taxes. See also Lewis v. Reynolds, 284 U.S. 281 (1932).

Under certain circumstances, the mitigation provisions of sections 1311 through 1314 allow adjustments to be made to a year even though the statute of limitations for that year has expired. For the mitigation provisions to apply, the following four conditions must be satisfied:

1) a determination must establish that the treatment in another year was incorrect;

2) correction of the error in the other year must be barred;

3) the party successful in the determination must have asserted a position inconsistent with a position adopted in the barred year; and

4) the determination must result in one of seven specific circumstances (e.g., double allowance of a deduction).

I.R.C. § 1311. Since all four conditions must be satisfied for mitigation to apply,[9] it is sufficient to merely note that the third requirement mentioned above is not satisfied.[10] An inconsistent position was not maintained by the taxpayer. I.R.C. § 1311(b)(1)(B); Treas. Reg. § 1.1311(b)-1(c)(2)(example). Therefore, the mitigation provisions do not permit the assessment of the depreciation adjustments for the years [redacted] and [redacted].[11]

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[9]When dealing with 2 specific circumstances (double exclusion from gross income and double disallowance of deduction/credit), neither of which is applicable to the situation at hand, the third condition listed above is not applicable.

[10]It also does not appear that the action which generated the depreciation adjustments in issue constitutes a "determination" as defined in section 1313(a). The adjustments did not result from a Tax Court decision, a closing agreement, a final disposition of a refund claim, or a "determination" agreement. Thus, the first condition, a determination, is not satisfied. Satisfaction of the final condition is also questionable (the existence of one of the seven specific circumstances [e.g., allowance of a double deduction]).

[11]Entering into closing agreements in addition to the Forms 870-P **may** make it possible to adjust the [redacted] and [redacted] years for

However, it must be noted that basis is adjusted for the amount of depreciation allowed or allowable in prior years. I.R.C. § 1016(a)(2). Therefore, if the adjustments are not made in the years [redacted] and [redacted], basis is nevertheless adjusted for the excessive depreciation. Thus, this becomes a timing matter.

If any part of an administrative adjustment request filed by the tax matters partner is not allowed, the tax matters partner may file a petition with respect to the partnership items to which such part of the request relates. I.R.C. § 6228(a)(1). As a general rule, the petition may be filed only after the expiration of 6 months from filing the request and before the date which is 2 years after the date of the request. I.R.C. § 6228(a)(2)(A). No petition may be filed after a NBAP with respect to the partnership taxable year is mailed (I.R.C. § 6228(a)(2)(B)), unless the NBAP is mailed prior to the expiration of the 2-year period following the filing of the request and the Service fails to mail an FPAA with respect to the partnership taxable year to which the request relates within the statutory period for assessment. In such case, the 2-year period for filing a petition does not expire before the date 6 months after the expiration of the period for assessment. I.R.C. § 6228(a)(2)(C). The 2-year period for filing a petition can be extended by agreement in writing between the Service and the tax matters partner. I.R.C. § 6228(a)(2)(D). No petition with regard to an administrative adjustment request can be filed after an FPAA for the same partnership taxable year has been timely mailed to the tax matters partner. I.R.C. § 6228(a)(3)(A)&(C).

Since the statute of limitations on assessment has not expired with respect to the years [redacted] through [redacted], the Service has a choice of actions provided all partners do not enter into

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the depreciation. The matter of whether a closing agreement determining tax liability for barred years is effective and enforceable is not clearly covered by the statute, regulations or judicial precedent. However, existing authority indicates that such an agreement is valid. See Dubinsky v. Becker, 64 F.2d 601 (8th Cir. 1933). The closing agreements, however, would have to specifically address the statute of limitations problem as well as the adjustments and interest on the resulting deficiencies. See IRM 8.13.1.7.1. In the event the parties wish to seriously consider this approach, please advise and we will explore this possibility further. As discussed above, all partners are entitled to request consistent settlement terms.

comprehensive agreements resolving all partnership items.[12] The Service can issue an FPAA[13] prior to [redacted], the present statute of limitations on assessment for the years. In such case, a petition for readjustment of the partnership items from the determination in the FPAA can be filed in court. A court with which a petition is filed shall have jurisdiction to determine all partnership items of the partnership for the partnership taxable year to which the FPAA relates. I.R.C. § 6226(f). Therefore, even partnership items not raised or examined during the audit (e.g., research credit) can be considered by the court if properly raised in the petition filed from the FPAA.[14]

If the Service decides not to issue an FPAA for the years [redacted] through [redacted], the tax matters partner can file an action with respect to the AARs any time during the 6-month period beginning [redacted] (the day after the expiration of the period described in section 6229(a) including extensions). I.R.C. § 6228(b)(2)(D). As mentioned above, any such action is limited to the partnership items requested in the AAR and any offsetting items raised by the Service. It should be noted, however, since the statute of limitations for assessment has been extended by agreement, the time period for filing requests for administrative adjustment of partnership items has also been extended. As a general rule, an AAR must be filed before the mailing of an FPAA and within 3 years after the later of the date the partnership return is filed or the last day for filing the partnership return (without regard to extensions). I.R.C. § 6227(a). This period for filing an AAR is extended for the period within which an assessment may be made pursuant to an agreement under section 6229(b), and for 6-months thereafter. I.R.C. § 6227(b). Therefore, other issues (e.g., research

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[12]As mentioned above, if all partners settle all partnership items, the partnership matter is completely resolved and no further partnership action can be taken. The Service's choice of actions differs for the years [redacted] and [redacted].

[13]The FPAA would include all partnership item adjustments for which there has not been a final settlement with all partners. Since the [redacted] issue was examined, it should also be included in the FPAA.

[14]Thus, even if the [redacted] issue is not addressed in the FPAA, the issue can be considered and decided by the court. In fact, that is the only way it can be decided, because the tax matters partner cannot file a petition regarding an AAR after an FPAA is timely issued. I.R.C. § 6228(a)(3)(A)&(C).

credit) can be raised through additional timely filed AARs.

As mentioned above, the statute of limitations for assessing taxes with respect to partnership items for the [redacted] and [redacted] tax years has expired. Therefore, the Service cannot issue an FPAA for such years. It is also too late for the partnership and/or its partners to file any additional administrative adjustment requests for the two years. However, the tax matters partner did timely file AARs for the 2 years [redacted] and [redacted] on [redacted], and [redacted], respectively. The Service issued NBAPs for [redacted] and [redacted] on [redacted], and [redacted], respectively. Under section 6228(a)(2)(B), no petition with respect to the AARs may be filed after the mailing of the NBAPs.[15] However, this limitation does not apply because the Service was unable to issue an FPAA within the period specified in section 6229(a). I.R.C. § 6228(a)(2)(C). Therefore, the general 2-year period for filing a petition regarding the AAR is applicable.[16] Under section 6228(a)(2)(D), this 2-year period can be extended by written agreement. Forms 9248 for the years [redacted] and [redacted] have been timely executed by the Service and the tax matters partner. The first Form 9248 was executed for both years [redacted] and [redacted] on [redacted]. Forms 9248 were continually executed for the two taxable years, extending the period in which to file petitions to [redacted]. Thus, the tax matters partner can file a petition with a court with respect to the AARs on or before [redacted]. The court's jurisdiction is limited to the issues raised in the AARs and not allowed by the Service and any offsetting issues raised by the Service.[17]

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[15]It is questionable whether the NBAPs which were issued after the assessment period had expired are valid for purposes of section 6228(a)(2)(B).

[16]For such a situation, I.R.C. § 6228(a)(2)(C) provides a special time period in which to file a petition (the 2-year period shall not expire before the date 6-months after the expiration of the section 6229(a) assessment period). However, this special period is not applicable, because under the facts of this case the general 2-year period is longer.

[17]Thus the tax matters partner cannot raise additional issues (e.g., research credit).

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as attorney client privilege. If disclosure becomes necessary, please contact this office for our views. Also, if you have any questions regarding the above, please feel free to contact the undersigned at 216-522-3380 (ext. (b)(6) .

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